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In the Supreme Court

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United States

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CHARLES ELMORE CROPLEY

OCTOBER TERM, 1941

No. 61

HARRY F. MEILINK, as Trustee in Bankruptcy, of the Estate of United Lamp & Shade Corp. (a corporation), Bankrupt,

Petitioner,

vs.

UNEMPLOYMENT RESERVES COMMISSION OF THE STATE OF CALIFORNIA,

Respondent.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Ninth Circuit.

BRIEF FOR RESPONDENT.

EARL WARREN,
Attorney General of the State of California,

JOHN J. DAILEY,
Deputy Attorney General of the State of California,
606 State Building, San Francisco, California,

Counsel for Respondent.

MAURICE F. McCAFFREY,
1025 "P" Street, Sacramento, California,

Of Counsel.

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BRIEF FOR RESPONDENT.

OPINION BELOW.

The opinion of the Circuit Court of Appeals for the Ninth Circuit is reported in 116 Fed. (2d) 330.

JURISDICTION.

As stated by petitioner, the jurisdiction of this Court is invoked under Section 240, as amended, of the Judicial Code, 28 U. S. C. A. 347.

QUESTION PRESENTED.

Is interest at the rate of 12 per cent per annum imposed on delinquent unemployment taxes pursuant to Section 45 of the Unemployment Reserves Act of California, and included in respondent's proof of claim, a penalty in bankruptcy within the purview of Section 57j of the Bankruptcy Act, where such rate is within the legislative power to fix and is expressly denominated as interest by the statute?

STATUTES INVOLVED.

Section 45 of the Unemployment Reserves Act (Chap. 352, Statutes of California 1935) as originally enacted reads as follows:

> "If any employer defaults in any payment required of him, for himself or on behalf of employees under this act, he shall become additionally liable for interest on such payments at the rate of twelve per cent per annum from the date such payment becomes due, both principal and interest being payable in the same manner as the contributions. Such payment and interest shall be collectible in the name of the fund in any manner practicable, including civil action by the commission against the defaulting employer."

Effective August 27, 1937, said Section 45 was amended (Chap. 752, Statutes of California 1937) to read as follows:

> "If any employer fails to make any payment required of him, or fails to deduct and pay to the commission the contributions of his workers, in accordance with the provisions of this act and of the rules and regulations adopted by the commission, he shall become additionally liable for interest on such payments at the rate of twelve per cent per annum from the date such payment becomes due, both principal and interest being payable in the same manner as the contributions. Such payment and interest shall be collectible in the name of the commission in any manner practicable, including civil action by the commission against the defaulting employer."

Effective September 19, 1939, Section 45 was again amended (Chap. 630, Statutes of California, 1939), to change the rate of interest from 12 per cent per annum to one per cent per month or fraction thereof.

Effective September 19, 1939, Section 45.3 was added (Chap. 630, Statutes of California, 1939), to the Unemployment Reserves Act to read as follows:

> "Any employer without good cause failing to pay any contribution within the time required by this act, or the rules and regulations of the commission, shall pay in addition thereto *a penalty of 10 per cent* of the amount thereof together with interest on said contributions at the rate prescribed in this article. If the failure to pay on the part of the employer is due to intentional fraud, *an additional penalty of 15 per cent* may be assessed against, and collected from, such de-

faulting employer. In any proceeding in court brought to enforce the provisions of this section, the finding of the commission that there exists no good cause excusing the delinquency, or that the failure of the employer is due to intentional fraud shall be for all purposes prima facie evidence of the existence of such facts." (Italics supplied.)

For the period during which interest accrued on unemployment taxes, as claimed by the respondent, Section 57j of the Bankruptcy Act (Title 11, U. S. C. A. Sec. 93j) provides:

"Debts owing to the United States, a State, a county, a district, or a municipality as a penalty for forfeiture shall not be allowed except for the amount of the pecuniary loss sustained by the act, transaction, or proceeding out of which the penalty or forfeiture arose, with reasonable and actual costs occasioned thereby and such interest as may have accrued thereon according to law."

Section 64a (4) of the Bankruptcy Act (Title 11, U. S. C. A. Sec. 104) reads as follows:

"The debts to have priority, in advance of the payment of dividends to creditors, and to be paid in full out of bankrupt estates, and the order of payment, shall be

* * * * * * *

"(4) Taxes legally due and owing by the bankrupt to the United States or any State or any subdivision thereof * * *."

The Constitution of the State of California, Article XX, Section 22, since its adoption in 1934, reads as follows:

"The rate of interest upon the loan or forbearance of any money, goods or things in action, or on accounts after demand or judgment rendered in any court of the State, shall be seven per cent per annum but it shall be competent for the parties to any loan or forbearance of any money, goods or things in action to contract in writing for a rate of interest not exceeding ten per cent per annum.

"No person, association, copartnership or corporation shall by charging any fee, bonus, commission, discount or other compensation receive from a borrower more than ten per cent per annum upon any loan or forbearance of any money, goods or things in action.

"However, none of the above restrictions shall apply to any building and loan association as defined in and which is operated under that certain act known as the 'Building and Loan Association Act,' approved May 5, 1931, as amended, or to any corporation incorporated in the manner prescribed in and operating under that certain act entitled 'An Act defining industrial loan companies, providing for their incorporation, powers and supervision,' approved May 18, 1917, as amended, or any corporation incorporated in the manner prescribed in and operating under that certain act entitled 'An act defining credit unions, providing for their incorporation, powers, management and supervision,' approved March 31, 1927, as amended, or any duly licensed pawnbroker or personal property broker, or any bank as defined in and operating under that certain act known as the 'Bank Act,' approved March 1, 1909, as amended, or any bank created and operating under and pursuant to any laws of this State or

of the United States of America or any nonprofit cooperative association organized under Chapter 4 of Division VI of the Agricultural Code in loaning or advancing money in connection with any activity mentioned in said title or any corporation, association, syndicate, joint stock company, or partnership engaged exclusively in the business of marketing agricultural, horticultural, viticultural, dairy, live stock, poultry and bee products on a cooperative nonprofit basis in loaning or advancing money to the members thereof or in connection with any such business or any corporation securing money or credit from any Federal intermediate credit bank, organized and existing pursuant to the provision of an act of Congress entitled 'Agricultural Credits Act of 1923,' as amended in loaning or advancing credit so secured, nor shall any such charge or any said exempted classes of persons be considered in any action or for any purpose as increasing or affecting or as connected with the rate of interest hereinbefore fixed. The Legislature may from time to time prescribe the maximum rate per annum of, or provide for the supervision, or the filing of a schedule of, or in any manner fix, regulate or limit, the fees, bonus, commissions, discounts or other compensation which all or any of the said exempted classes of persons may charge or receive from a borrower in connection with any loan or forbearance of any money, goods or things in action.

"The provisions of this section shall supersede all provisions of this Constitution and laws enacted thereunder in conflict therewith."

STATEMENT.

Respondent accepts the statement of the case set forth by petitioner on pages 4 and 5 of his brief. For the sake of uniformity, the terms Unemployment Reserves Act and Unemployment Reserves Commission will be used in this brief, although by amendments effective September 19, 1939, the title of the statute was changed to Unemployment Insurance Act and the name of the Respondent-Commission was changed to California Employment Commission.

SUMMARY OF ARGUMENT.

Interest at the rate of 12 per cent per annum, or one per cent per month, on delinquent taxes does not constitute a penalty in bankruptcy where there is no statutory ambiguity to resolve and the legislature fixed the rate of interest to be imposed because of the delay in the payment of the tax after delinquency.

Interest at the rate of 12 per cent per annum is neither excessive nor arbitrary; nor is it in excess of rates of interest allowed to be charged by private parties in California. The measure of compensation to the State for delay in payment of unemployment taxes was fixed by the California Legislature in Section 45 of the Unemployment Reserves Act.

The California Legislature is unhampered by any constitutional limitation in fixing rates of interest on delinquent taxes. It may fix varying rates of interest on different kinds of taxes. Section 45 of the Cali-

fornia Unemployment Reserves Act is free from ambiguity and expressly denominates 12 per cent per annum as interest.

ARGUMENT

I.

INTEREST AT THE RATE OF 12 PER CENT PER ANNUM IMPOSED BY SECTION 45, CALIFORNIA UNEMPLOYMENT RESERVES ACT, ON DELINQUENT TAXES IS NOT A PENALTY IN BANKRUPTCY.

The sole question presented in this case is whether the 12 per cent interest on delinquent taxes provided for in Section 45 of the California Unemployment Reserves Act is allowable as interest in bankruptcy or whether the same constitutes a penalty not allowable under Section 57j of the Bankruptcy Act. (Title 11, U. S. C. A. Sec. 93j.)

There is a clear distinction between interest on the one hand and penalty on the other. As stated by this Court in *United States v. Childs*, 266 U. S. 304, a penalty is a means of punishment, while interest is a means of compensation for delay in payment. A penalty arises upon the act of delinquency; it arises but once. The amount thereof ordinarily is not reduced if the tax is paid shortly after delinquency. In other words, a penalty is a pecuniary punishment for an infraction of the law—failure to pay the tax on its due date—and the amount thereof ordinarily has no relation to the extent of the delay beyond the statutory period. Interest, on the other hand, is a continu-

ing obligation—it accrues upon the date of delinquency and continues as long as the tax remains unpaid. Its purpose is to compensate the State for the loss occasioned to it by the delay in payment.

In *United States v. Childs*, supra, this Court held that interest at the rate of one per cent per month imposed for delinquency in tax payment by the Revenue Act of 1916 did not constitute a penalty within the meaning of Section 57j of the Bankruptcy Act. After quoting from the opinion of the Circuit Court (*In Re J. Menist & Co.*, 290 Fed. 947 which was the *Childs* case below), holding such interest to be a penalty, this Court stated, at page 309:

> "We are unable to concur. It makes the rate of interest that of a particular locality, differing with the locality—in New York, as said by the government, 6 per cent; in the Middle West, 8 per cent; and on the Pacific Coast, 10 per cent—and abridges or controls a federal statute by a local law or custom, and takes from it uniformity of operation. Besides, the federal statute is precise, and it is made peremptory by the distinction between 'penalty' and 'interest' and if it may be conceded that the use of the latter word would not save it from condemnation if it were in effect the former, it cannot be conceded that 1 per cent per month—12 per cent a year—gives it that illegal effect, certainly not against legislative declaration that is within the legislative power, there being no ambiguity to resolve."
>
> * * * * * * *
>
> "The tax in this case is one on income; a burden imposed for the support of the government. In-

> terest is put upon it and so denominated, distinguished from the 5 per cent as penalty, clearly intended to compensate the delay in payment of the tax—the detriment of its nonpayment, to be continued during the time of its nonpayment—compensation not punishment."

This Court in distinguishing its decision in the *Childs* case from its earlier decision in *New York v. Jersawit*, 263 U.S. 493, had this to say at 266 U.S. 309:

> "To this conclusion New York v. Jersawit, 263 U.S. 493, 44 S. Ct. 167, 68 L. Ed. 405, is not antagonistic. There a statute of New York (Consol. Laws, c. 60) was passed on which required 'every domestic corporation' to 'annually pay in advance * * * an annual franchise tax' upon its net income for the year next preceding, and provided that, if the tax were not paid, the corporation should pay 'in addition to the amount of such tax * * * ten per centum of such amount, plus one per centum for each month the tax * * * remains unpaid.' This liability the lower federal courts pronounced a penalty and not to be allowed. In that conclusion this court concurred and decided that, being penalty, it was disallowed by Bankruptcy Act, Sec. 57j. And this not only because the 1 per centum was 'more than the value of the use of the money', but because it was added by the statute to the 10 per cent, to make a single sum, and 'must be treated as part of one corpus, and must fall with that.' "

It is important to observe that in the *Jersawit* case the statute provided for the payment by the taxpayer

of "ten per centum of such amount (annual franchise tax), plus one per centum for each month the tax remained unpaid." *The statute thus did not denominate the one per cent as being interest,* and this Court held that because the one per cent was added to the 10 per cent to make a single sum, it "must be treated as a part of one corpus, and must fall with that." But in the case now before the Court, the California Legislature clearly and expressly fixed an interest rate of 12 per cent per annum during the period of delinquency and it did not add or couple this interest with any penalty provisions, such as the 10 per cent and 15 per cent penalties set forth in Section 45.3 of the Unemployment Reserves Act, which provisions became effective September 19, 1939.

United States v. Childs, supra, so far as respondent can determine, has never been limited by any subsequent decision of this Court. On the contrary, it has been followed and cited with approval by the Second and Seventh Circuit Courts of Appeals, as well as by the Ninth Circuit Court in its opinion in the instant case below.

In the case of *In re Semon,* 80 Fed. (2d) 81, the Second Circuit Court held that interest at the rate of one per cent per month on delinquent taxes under the Revenue Act of 1928 did not constitute a penalty in bankruptcy. The Circuit Court stated, at page 82:

> "An interest rate of one per cent a month is not per se a penalty. United States v. Childs, 266 U.S. 304, 45 S. Ct. 110, 69 L. Ed. 299."

The *Childs* and *Semon* cases were followed in the case of *In re Beardsley & Wolcott Mfg. Co.* (2 C.C.A.), 82 Fed. (2d) 239, wherein it was held that interest at the rate of three-fourths of one per cent per month imposed by statute upon delinquent city real estate taxes did not constitute a penalty in bankruptcy.

In the case of *In re Martin* (7 C.C.A.), 75 Fed. (2d) 618, it was held that interest on unpaid taxes at the rate of one per cent per month imposed by the Illinois Motor Fuel Tax Act was not a penalty in bankruptcy. At page 621, the Circuit Court stated:

> "The matter of interest rates is within the power of the legislature. People v. Baldwin, 287 Ill. 87, 122 N.E. 148. We find nothing in the record to indicate anything grossly excessive or inequitable in the interest fixed by the statute and carried into the judgment, and we are not at liberty to disturb its allowance."

In the case of *In re Kallak* (D. C. North Dakota), 147 Fed. 276, decided in 1906, it was held that interest at one per cent per month on unpaid property taxes imposed by a state statute did not constitute a penalty in bankruptcy.

New York v. Jersawit, 266 U.S. 493, strongly relied upon by the petitioner throughout his brief, is so clearly distinguishable that it does not substantiate the contention of the petitioner in any respect. As pointed out above, this Court in the *Childs* case clearly distinguished its decision in the *Jersawit* case. Furthermore, the statute involved in the *Jersawit* case did not denominate any charge as *interest* on the delin-

quency of tax payments. It is illogical to argue that the *Jersawit* case and not the *Childs* case is controlling here because the former involved a state statute while the latter involved a federal statute. There is no valid reason why the measure of compensation for tax delinquencies should be higher to the Federal Government than to a State. Moreover, the California Legislature, like the Federal Congress, is unfettered by any constitutional limitation in fixing rates of interest on delinquent taxes.

As stated by the Ninth Circuit Court in its opinion below, the only decision of a Circuit Court of Appeals contrary to the respondent's contention is *In re Pressed Steel Car Co. of New Jersey* (3 C.C.A.), 100 Fed. (2d) 147. In holding interest at the rate of one per cent per month on state corporation franchise taxes to be a penalty, the Third Circuit Court relied solely upon the *Jersawit* case; the Circuit Court did not cite or distinguish the decision of this Court in the *Childs* case nor the decisions of the Seventh and Second Circuit Courts in the *Martin* and *Semon* cases and in fact assumed that the state would be content with simple interest for the issue was not sharply contested.

The case of *In re Ashland Emery and Corundum Co.* (D.C. Mass.), 229 Fed. 829, relied upon by petitioner at pages 10, 12 and 16 of his brief, was in effect overruled by this Court in *United States v. Childs*, 266 U.S. 304, 308, when it said in commenting upon the decision of the Circuit Court of Appeals in the case of *In re J. Menist and Co.*, 290 Fed. 947:

"The Circuit Court of Appeals adjudged the tax in the present case a debt and assigned against it interest at 6 per cent; the court considering that that interest was compensation for the delinquency anything in excess becoming penalty and within the prohibition of section 57j. The court said:

'On the point at bar (1 per cent interest as the price of the delay being penalty) we are in accord with In re Ashland, etc. (D.C.) 229 Fed. 829, and hold that, there being no evidence of any injury or damage to the government by the withholding of this tax, except that which flows from the nonpayment of a just debt, anything in excess of the legal rate of interest is to be treated as a penalty and not allowed.'

"We are unable to concur. * * *"

In the case of *In re 168 Adams Building Corporation* (D.C. Ill.), 27 Fed. Supp. 247, aff'd. 105 Fed. (2d) 704 (C.C.A. 7), cert. denied, 308 U.S. 623, also relied upon by petitioner on page 17 of his brief, the ruling of the District Court on interest was not contested on appeal and the opinion of the Seventh Circuit Court is entirely silent thereon. The respondent respectfully submits that had the Circuit Court's attention been directed to the matter of interest it would have followed its ruling in the *Martin* case, supra.

The decision of the District Court in the Second Circuit, in the case of *In re A. E. Fountain, Inc.* (D.C. N.Y.), 295 Fed. 873 (cited at page 18 of petitioner's brief), was in effect overruled by the later decisions of the Second Circuit Court in the *Semon* and *Beardsley & Wolcott* cases, supra.

The case of *In re Wells* (D.C. Md.), 4 Fed. Supp. 329, cited on page 18 of petitioner's brief is not in point, since there no claim was made for interest or penalties.

Petitioner, on page 19 of his brief, attempts to distinguish the case of *In re Martin* (7 C.C.A.), 75 Fed. (2d) 618, on the ground that the Court, in its opinion, failed to mention or discuss Section 57j. As pointed out by the Ninth Circuit Court in its opinion below, reference to the briefs in the *Martin* case shows that the appellant therein directed the Court's attention to Section 57j of the Bankruptcy Act. Nevertheless we submit that the Court in allowing interest at the rate of 1 per cent per month necessarily held that such rate of interest was not a penalty under Section 57j of said Act.

In this connection, it should be noted that the decision of the Second Circuit Court in the case of *In re J. Menist & Co.*, 290 Fed. 947, holding interest at one per cent per month to be a penalty in bankruptcy, was reversed by this Court on appeal in *United States v. Childs*, supra.

II.

THE LEGISLATURE MAY PROVIDE FOR INTEREST ON DELINQUENT TAXES AND MAY FIX THE RATE THEREOF.

While delinquent taxes do not bear interest unless so provided by statute, the legislature may provide therefor and may fix the rate in the absence of any constitutional limitation, of which there is none in the

Constitution of the State of California, 24 *California Jurisprudence* 296; *United States v. Childs,* 266 U.S. 304; *In re Martin* (7 C.C.A.), 75 Fed. (2d) 618; *In re Semon* (2 C.C.A.), 80 Fed. (2d) 81.

In Section 45 of the California Unemployment Reserves Act the legislature, presumably after consideration of all factors involved, fixed the measure of compensation to the State for delay in payment of unemployment taxes. The legislative intent and purpose should not be subverted by the Courts through the device of labeling a penalty that which the legislature has declared to be interest—certainly not where the legislative declaration is neither arbitrary nor unreasonable. As stated in the opinion of the Ninth Circuit Court below, "To fix a rate of interest other than that fixed by law would be a departure from the legislative mandate in the sphere in which the legislature is supreme."

From an inspection of the tax statutes in effect in California prior to the enactment of the California Unemployment Reserves Act, it cannot be doubted that the California Legislature was well aware of the distinction between interest and penalty; and it is to be presumed that the legislature had knowledge of the principles enunciated in the *Jersawit* and *Childs* cases. (*Chesapeake & Potomac Tel. Co. v. Manning,* 186 U.S. 238.) It was undoubtedly due to this knowledge that the legislature, when in 1939 it added the common 10 per cent negligence and 15 per cent fraud penalties to the Unemployment Reserves Act, placed such penalties in a separate section of the Act entirely apart from the

section providing for interest on delinquent tax payments. It is indeed *startling* that petitioner should in effect ask this Court to impute to the legislature some ulterior motive in providing this separability between the statutory interest and penalty provisions (see page 12 of petitioner's brief). A Court may not impute a particular intention to the legislature when nothing in the language employed implies such an intention.

It may be conceded that, as argued by petitioner on page 10 of his brief, a true penalty may not be converted into interest merely by calling it interest. On the other hand, while statutory nomenclature is not conclusive it is of probative force. *In re Beardsley & Wolcott Mfg. Co.* (2 C.C.A.), 82 Fed. 239. There must of necessity be a fundamental assumption that the language used in a statute expresses the legislative intent, particularly when, as here, that language is entirely free from ambiguity.

In the *Childs* case, this Court pointed out that the fixing of a rate of interest on delinquent taxes was a matter within the legislative power, and to construe Section 57j of the Bankruptcy Act so as to permit this statutory rate to be ignored would result in the substitution of a rate which would be dependent in each case upon the value of the use of money in different localities. Both of these observations apply with equal force in the instant case.

Here, the California Legislature, acting within its sphere of authority, has fixed a rate of interest on delinquent taxes and has denominated it as interest, and, as will be shown later herein, the Legislature has

fixed a rate of interest which is less than the maximum rate allowed to be charged by private parties in the State of California.

To depart from this rate of interest fixed by legislative mandate would result in a lack of uniformity of operation. As stated in the opinion of the Court below:

> "* * * for not only might a different rate be fixed in California, but different rates might be fixed in the same community by different referees in bankruptcy or by the same referee if in his judgment the value of the use of money had fluctuated from time to time in the community in which he was exercising his judicial functions."

The application of this principle of uniformity of interpretation is not limited to the State of California. Unemployment Insurance is a national program. Each of the forty-eight states, as well as Alaska, Hawaii, and the District of Columbia, has on its books an unemployment compensation statute. In thirty-eight jurisdictions the unemployment compensation statutes impose interest at the rate of one per cent per month on delinquent unemployment taxes. Accordingly, it is submitted that the reasoning of this Court in the *Childs* case is equally pertinent in the case now before the Court.

III.

THERE IS NO CONSTITUTIONAL LIMITATION UPON THE POWER OF THE CALIFORNIA LEGISLATURE TO FIX THE RATE OF INTEREST ON DELINQUENT TAX PERIODS. THE STATUTORY RATE OF INTEREST HERE INVOLVED IS NEITHER EXCESSIVE NOR INEQUITABLE.

At page 19 of his brief, petitioner contends that section 22, Article XX, of the California Constitution limits the power of the legislature to impose interest on delinquent tax obligations to seven per cent. It is submitted that a plain construction of Section 22 indicates clearly that the enactment is applicable to private parties and does not affect the state.

Section 22 sets up three catagories of obligations to which its inhibitions apply. These are:

> 1. "Upon the loan or forbearance of any money, goods or things in action * * * but it shall be competent for the parties to any loan or forbearance to contract in writing for a rate of interest not exceeding ten per cent per annum."
>
> 2. On accounts after demand.
>
> 3. On judgments rendered in any court of the State.

It is clear that delinquent taxes do not come within the first category. A tax is not founded upon contract and does not depend for its validity upon the individual assent of the taxpayer. It has long been held in California that a tax is not a debt due and does not establish a debtor-creditor relationship. 24 *California Jurisprudence* 21. Both loans and forbearances are premised on a contract or debtor-creditor

relationship. *Title Guaranty and Surety Co. v. Klein*, 178 Fed. 689.

With respect to the second category, Bouvier's Law Dictionary (Baldwin's Century Edition), page 33, defines account as: "A detailed statement of the mutual demands in the nature of debt and credit between parties, arising out of contracts or some fiduciary relation". Since an account is premised on a debtor-creditor relationship, and since a tax is not a debt and does not arise out of a contract or fiduciary relationship, it is submitted that the second classification imposes no inhibition on the legslative power to set interest rates on delinquent taxes.

With respect to the third category, it should suffice to say that a constitutional limitation of the rate of interest on judgments cannot be considered as an inhibition on the legislative power to set the interest rate on delinquent taxes. Judgments, including judgments for taxes, have borne interest at 7 per cent in California since 1868, independently of anything contained in section 22, Article XX. (Statutes of California, 1868, page 553; Civil Code, Section 1920, enacted March 21, 1872; superseded by Statutes of California, 1919, page lxxxiii.) Section 22, Article XX, on the other hand, was not enacted until 1934. However, the point is of no more than academic interest in the case now before this Court, since the tax claim here in issue has never been reduced to judgment.

Section 22 expresses itself fully on the matter of the interest rate permitted on numerous types of obliga-

tions. Nowhere does it speak on the subject of tax delinquencies. There are several thousand taxing agencies exercising their respective powers within the State of California. Surely, had the legislature intended section 22 to limit its power with respect to interest on delinquent taxes, it would have framed the enactment accordingly. With respect to petitioner's contention, the silence of section 22 on the subject of interest on delinquent taxes is peculiarly significant. That silence, it is submitted, compels the conclusion that no such limitation was intended.

It is well settled that in the absence of express words to the contrary neither the State nor any of its agencies or subdivisions is included within the general words of a statute. *Estate of Miller,* 5 Cal. (2d) 588, 597, 55 Pac. (2d) 491; 23 *California Jurisprudence,* page 625, Sec. 24; see also, *Dollar Savings Bank v. U. S.,* 19 Wall. 227, 86 U. S. 227. The rules of construction by which the meaning of language is to be ascertained are the same as respects constitutional or statutory provisions. *Winchester v. Mabury,* 122 Cal. at 527, 55 Pac. 393. At 16 *Corpus Juris Secundum,* page 140, section 70, it is stated that a state constitution is construed strictly in favor of the state, and as not divesting it or its government of any of its prerogatives, unless the intent to do so is clearly expressed. Therefore, it is to be concluded that section 22 of Article XX of the California Constitution in no wise limits the powers of the State legislature to fix the rate of interest on delinquent taxes, for nowhere in said constitutional provision is there an

expressed intention that the State shall be bound thereby.

It is to be noted that, at the time the Legislature in 1933 proposed Article XX, section 22 of the Constitution by Assembly Constitutional Amendment 79, during the same session, July 31, 1933, more than two months thereafter, the Retail Sales Tax Act was enacted (Statutes of California, 1933, p. 2599), and under section 22 thereof provided for interest at the rate of 12 per cent per annum on delinquent sales tax payments.

Again, the Personal Income Tax Act (Deering's Act 8494, section 15), from its enactment in 1933 until amended in 1935, provided for interest at the rate of one per cent per month on delinquent taxes.

Furthermore, the Bank and Franchise Tax Act (Deering's Act 8488, section 24) during the years 1931 to 1937, provided for interest on delinquent taxes at the rate of one per cent per month.

As pointed out herein, section 45 of the Unemployment Reserves Act (Chap. 352, Statutes of California, 1935) provided for interest at the rate of 12 per cent per annum on delinquent taxes.

This course of legislative conduct, which took place both before, during and subsequent to the submission of Assembly Constitutional Amendment 79, indicates clearly that the Legislature, in the language which it used in framing section 22, Article XX of the Constitution did not intend in any way to limit its power to fix varying rates of interest on delinquent tax payments.

Petitioner stresses the fact that the interest rate imposed by the Unemployment Reserves Act is in excess of the interest rate on unpaid judgments. (Petitioner's brief, page 19.) There is no basis in California legislative history for lumping the interest rate on unpaid judgments with that on unpaid taxes, or for applying the interest rate on judgments to delinquent taxes.

The interest rates on California taxes, have always been contained in the individual taxing statutes and have been and are calculated at varying rates. Interest on taxes, as distinguished from interest on judgments, has traveled an entirely separate statutory path. There is no basis in law or in fact for petitioner's contrary contention in this regard. Indeed, a survey of California state laws compels the conclusion that the interest rate on judgments has no connection whatsoever with the interest rate on unpaid taxes.

Petitioner contends that an interest rate in excess of that permitted to private persons is *ipso facto* a penalty as to the excess. (Petitioner's Brief, page 13.) Section 22, Article XX of the Constitution expressly exempts from its operation certain types of lenders such as building and loan associations, loan companies, credit unions, banks, and any duly licensed pawnbrokers and personal property brokers. The Legislature was given power to prescribe rates for the categories which were exempted from the constitutional limitation.

In California, credit unions may, by law, charge interest on loans at the rate of one per cent per

month. (Deering's Act 1887, section 3, subdivision 5.) Pawnbrokers may charge up to 2 per cent per month on the first $100 of indebtedness, and one per cent per month on anything above that amount. (Deering's Act 5826, section 2, as amended 1939.) Personal property brokers may charge interest at 2½ per cent per month on the unpaid balance not in excess of $100, and up to 2 per cent per month on the remainder. (Deering's Act 5825 (2d), section 17, as amended, 1939.)

Thus it will be seen that the interest provision here under attack is *not* in excess of the interest rate which California law permits many classifications of creditors to impose. It could hardly be maintained, for example, that the 2 per cent per month interest rate permitted to personal property brokers is in any sense a penalty. There is no more warrant for applying that label to the interest rate set up by the Unemployment Reserves Act.

In *Horn v. Boone County* (8 C. C. A.), 44 Fed. (2d) 920, the Court held that interest on delinquent taxes at 10 per cent per annum did not constitute a penalty in bankruptcy, inasmuch as the state (Nebraska) permitted private parties by agreement to fix a rate of interest as high as 10 per cent. As so aptly stated by the Ninth Circuit Court of Appeals in its opinion below:

> "If this rule be applied in California it would follow that 12 per cent is not a penalty because the laws of California permit an even higher rate than 12 per cent per annum with reference to certain types of loans."

In fixing the rate of interest here involved, the legislature undoubtedly had in mind the peculiar nature and purpose of the taxes levied by the statute. These unemployment taxes differ substantially from ordinary taxes; instead of being deposited in the general fund of the state, these taxes go into a special fund to be used *only* for the payment of benefits to qualified unemployed workers. Such taxes are not public funds in the sense that they are subject to appropriation for general state purposes. The California Unemployment Reserves Act provides for no lien to protect the collection of these taxes. The timely payment of these contributions is necessarily essential to the maintenance and success of the unemployment insurance program. The legislature, in fixing interest at the rate of 12 per cent per annum as the measure of compensation to the state for the loss occasioned by the delay in payment of contributions, must be assumed to have had in mind all of the circumstances and factors above discussed.

CONCLUSION.

It is respectfully submitted that the authorities cited and relied upon by respondent, and in particular the *Childs* case, clearly established the proposition that interest on delinquent unemployment taxes at the rate of 12 per cent per annum, as prescribed in section 45 of the California Unemployment Reserves Act, does not constitute a penalty within the meaning of section 57j of the Bankruptcy Act, such rate

being neither excessive nor unreasonable and not higher than the rate of interest allowed to be charged by private parties in the State of California.

Upon the foregoing considerations and authorities the decision of the Ninth Circuit Court of Appeals should be affirmed.

Dated, Sacramento, California,
December 5, 1941.

Respectfully submitted,

EARL WARREN,
Attorney General of the State of California,

JOHN J. DAILEY,
Deputy Attorney General of the State of California,

Counsel for Respondent.

MAURICE P. MCCAFFREY,
Of Counsel.

SUPREME COURT OF THE UNITED STATES.

No. 61.—October Term, 1941.

Harry F. Meilink, as Trustee in Bankruptcy of the Estate of United Lamp & Shade Corporation, Bankrupt. *vs.* Unemployment Reserves Commission of the State of California.	On Writ of Certiorari to the United States Circuit Court of Appeals for the Ninth Circuit.

[January 5, 1942.]

Mr. Justice Jackson delivered the opinion of the Court.

The petitioner is the trustee of a bankrupt which was indebted to the California Unemployment Reserves Commission for contributions which had accrued under the California Unemployment Reserves Act. Section 45 of that Act provided that in the event of default in payment of contributions due the employer "shall become additionally liable for interest on such payments at the rate of twelve per cent per annum from the date such payment becomes due, both principal and interest being payable in the same manner as the contributions." Deering's Cal. Stats. 8780d, § 45. The Commission filed proof of a priority claim in the bankruptcy proceeding for the principal amount of the accrued contributions and interest thereon at the rate of twelve per cent.

The trustee paid the principal sum with interest at six per cent, but refused to pay more, relying on § 57j of the Bankruptcy Act, 11 U. S. C. § 93j, which provides that "Debts owing to the United States, a State, a county, a district, or a municipality as a penalty or forfeiture shall not be allowed, except for the amount of the pecuniary loss sustained by the act, transaction, or proceeding out of which the penalty or forfeiture arose, with reasonable and actual costs occasioned thereby and such interest as may have accrued thereon according to law." The trustee asserted that any exaction in excess of six per cent, which he claimed was the "reasonable and customary rate of interest," was a penalty; the bankruptcy court decreed that all above seven per cent a common,

though not an invariable, legal rate in California) was a penalty and refused to allow so much of the claim; and the Circuit Court of Appeals for the Ninth Circuit reversed on the ground that no part of the twelve per cent was a penalty. 116 F. 2d 330. We granted certiorari because of the conflict between this decision and that of the Circuit Court of Appeals for the Third Circuit in *In re Pressed Steel Car Co. of New Jersey.*[1]

Petitioner seeks to establish that the twelve per cent exaction here in question is not "interest" by pointing to Article XX, Section 22 of the California Constitution, which provides that, except for specified institutions, the rate of interest on loans, and on accounts after demand or judgment, shall be seven per cent, and leaves the parties free to contract in writing for a rate not exceeding ten per cent.[2] We do not understand that as a matter of State law the California legislature was thereby forbidden to prescribe the higher rate here involved. And the mere difference in rates does not establish that the twelve per cent rate is not "interest" within the meaning of § 57j of the Bankruptcy Act.

It is common knowledge that interest rates vary not only according to the general use value of money but also according to the hazard of particular classes of loans. Delinquent taxpayers as a class are a poor credit risk; tax default, unless an incident of legitimate tax litigation, is, to the eye sensitive to credit indications, a signal of distress. A rate of interest on tax delinquencies which is low in comparison to the taxpayer's borrowing rate—if he can borrow at all—is a temptation to use the state as a convenient, if involuntary, banker by the simple practice of deferring the payment of taxes.

Another variable is the amount necessary to compensate for the trouble of handling the item. The legislature may include compensation to the state for the increased costs of administration in

[1] 100 F. 2d 147, certiorari denied *sub. nom.* Wick et al. v. New Jersey, 306 U. S. 648.

[2] This reads in part as follows:

"The rate of interest upon the loan or forbearance of any money, goods or things in action, or on accounts after demand or judgment rendered in any court of the State, shall be seven per cent per annum but it shall be competent for the parties to any loan or forbearance of any money, goods or things in action to contract in writing for a rate of interest not exceeding ten per cent per annum."

Expressly excepted are building and loan associations, industrial loan companies, credit unions, pawnbrokers, personal property brokers, State and National Banks, and cooperative associations.

the exaction for delay in paying taxes without thereby changing it from interest to penalty.

These factors—risk, and the expenses of handling—are reflected in the interest rates permitted by California to certain types of financial institutions: for example, credit unions may charge interest at the rate of one per cent per month;[3] pawnbrokers, at two per cent per month on the first one hundred dollars of indebtedness;[4] and personal property brokers, two and one-half per cent per month on the first three hundred dollars.[5] A differentiation of treatment for particular types of loans similar in principle is commonly made by other states.[6]

New York v. *Jersawit*, 263 U. S. 493, is thought by petitioner to require a decision in his favor. That case involved a New York statute visiting tax delinquents with an additional liability of ten per cent of the tax, and adding thereto a further liability of one per cent per month, which was not denominated interest. The Circuit Court of Appeals had held that such provision was penal, but had allowed interest at the usual legal rate on the theory that it represented actual damage. *In re Ajax Dress Co.*, 290 F. 959. This Court, speaking through Mr. Justice Holmes, said:

"There can be no doubt that the additional ten per centum charged for failure to pay by January 1 is a penalty, disallowed by the Bankruptcy Act, § 57j, but it is urged that the one per centum for each month of default is statutory interest and that the State is entitled to that and otherwise would be entitled to none. As the one per centum is more than the value of the use of the money and is added by the statute to the ten to make a single sum it must be treated as part of one corpus and must fall with that. We presume that in this event the State does not object to receiving the simple interest allowed. That part of the order will stand." 263 U. S. at 496.

Here the exaction computed according to lapse of time is not lumped together with another percentage computed without reference to lapse of time; here the exaction is denominated interest by the statute, and there it was not; and we cannot be so confident here that twelve per cent "is more than the value of the use of the money," or of the validity of the implied major premise

[3] Deering's Cal. Stats. 1887 § 3(5), as amended, 1939.

[4] Deering's Cal. Stats. 5826 § 2, as amended, 1939.

[5] Deering's Cal. Stats. 5825(2d) § 17, as amended, 1939.

[6] Clark, Financing the Consumer (1933), Appendix I.

that an exaction in excess of such value cannot be merely an interest charge.[7]

The decision which controls here is the more recent one of *United States* v. *Childs*, 266 U. S. 304, where the statute separately denominated a flat five per cent exaction as a penalty, and an additional one of one per cent a month as interest. The latter was held to be "interest" within the meaning of § 57j of the Bankruptcy Act. The distinction from the fact that the exaction in that case was by the United States and in this case by a State calls for no difference in result. We must give credit to a state legislature acting within its Constitutional sphere like that accorded to Congress acting in its Constitutional sphere. And the distinction which Congress made in the legislation considered in the *Childs* case and in other revenue legislation between penalty as a fixed *ad valorem* amount taking no account of time, and interest which does depend on time, is persuasive that its use of the word "penalty" in the Bankruptcy Act will bear a like differentiation from interest.

Finally, it may be observed that Congress itself has provided in the District of Columbia Unemployment Compensation Act that in the event contributions are not paid when due "there shall be added, as part of the contributions, *interest* at the rate of 1 per centum per month." (Italics supplied.) D. C. Code (Supp. V, 1939) tit. 8, § 314(e).

Affirmed.

Mr. Justice ROBERTS took no part in the decision of this case.

A true copy.

Test:

Clerk, Supreme Court, U. S.

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[7] Compare the following exactions, provided by the various Unemployment Compensation Acts for non-payment of contributions due:

"Interest" at 6% per annum or its equivalent on a monthly basis: United States, Delaware, Florida, Georgia, Indiana, Massachusetts, New York, North Carolina, Oregon, Utah, Wisconsin; at 8%: Ohio; at 81/100% per month: Kansas; at 9%: Connecticut, Michigan; at 12%: District of Columbia, Alabama, Arizona, Arkansas, Colorado, Illinois, Iowa, Louisiana, Maine, Maryland, Minnesota, Mississippi, Missouri, Montana, Nebraska, Nevada, New Hampshire, New Jersey, New Mexico, North Dakota, Oklahoma, Pennsylvania, Rhode Island, South Carolina, South Dakota, Tennessee, Vermont, Virginia, Washington, West Virginia, Wyoming.

"Penalty" at 12%: Kentucky, Texas; at 2% to 25% per month: Idaho.